

## Message Text

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PAGE 01 BRUSSE 08159 201705Z

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ACTION EUR-12

INFO OCT-01 EA-07 IO-13 ISO-00 AID-05 CIAE-00 COME-00

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AMEMBASSY TOKYO

AMEMBASSY VIENNA

USMISSION EC BRUSSELS

USMISSION GENEVA

USMISSION OECD PARIS

C O N F I D E N T I A L BRUSSELS 8159

E.O. 11652: GDS

TAGS: EFIN BE

SUBJECT: NATIONAL BANK CONTINUES FIRM BEHIND THE FRANC--BUT UNEASY  
ABOUT THE FUTURE

REF; BRUSSELS 7819

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PAGE 02 BRUSSE 08159 201705Z

1. SUMMARY. THE BELGIAN NATIONAL BANK IS CONTINUING ITS

FIRM SUPPORT FOR THE BELGIAN FRANC TO KEEP IT WITHIN SNAKE MARGINS VIS-A-VIS THE DM. IT IS EMPLOYING INTERNAL INTEREST RATE POLICY PLUS HEAVY MARKET INTERVENTION IN RECENT DAYS, NOW ESTIMATED AT AROUND BF 25 BILLION IN FECOM DRAWINGS. BANK GOVERNOR DE STRYCKER HAS PUBLICLY REITERATED THE GOVERNMENT'S DETERMINATION TO REMAIN WITHIN THE SNAKE, AND REFUSED TO PRESSURE THE FRG TO REVALUE. IN PRIVATE, HOWEVER, RESPONSIBLE OFFICIALS OF THE NATIONAL BANK ARE LESS OPTIMISTIC--DESPITE BELGIUM'S CONTINUING STRONG EXTERNAL POSITION, THERE IS APPREHENSION OVER THE EFFECTS OF A PROLONGED PERIOD OF HIGH INTEREST RATES ON THE COUNTRY'S ECONOMIC, SOCIAL AND POLITICAL SCENE. IF THE DANISH KRONE LEAVES THE SNAKE, ONE OFFICIAL PREDICTS GENERAL BENELUX RECONSIDERATION OF THEIR POSITIONS AS WELL, AT LEAST WITHIN EXISTING SNAKE ARRANGEMENTS. END SUMMARY.

2. DURING THE PAST TEN DAYS, THE BELGIAN NATIONAL BANK HAS FURTHER STRENGTHENED ITS SUPPORT FOR THE BELGIAN FRANC TO KEEP IT WITHIN SNAKE MARGINS. LAST WEEK IT RAISED THE CENTRAL BANK DISCOUNT RATE FOR THE SECOND TIME THIS SUMMER, FROM 8 TO 9 PERCENT. (ADVANCES BEYOND A CERTAIN QUOTA ARE AT A FLOATING RATE, NOW AT 11.5 PERCENT.) REGULATION OF PRIVATE BANK FOREIGN EXCHANGE DEALINGS IS VERY TIGHT; BANK SOURCES REPORT INTEREST RATES AROUND 30 PERCENT FOR ONE-MONTH CONVERTIBLE BELGIAN FRANCS, A THREE-FOLD JUMP SINCE LAST JUNE. TO REDUCE THE EFFECT OF LEADS AND LAGS, IMPORTERS ARE BEING OBLIGED TO MEET INVOICE TERMS STRICTLY; I.E., DELAY PAYMENTS UNTIL REQUIRED (THERE IS NO SPECIAL PRESSURE ON EXPORTERS TO LENGTHEN TERMS, HOWEVER). THE SPREAD BETWEEN THE COMMERCIAL AND FREE FINANCIAL RATES IN BELGIUM'S TWO-TIER MARKET HAS REACHED 4.5 PERCENT, A STILL TOLERABLE FIGURE.

3. IN RECENT DAYS, HOWEVER, THESE MEASURES HAVE PROVED INSUFFICIENT. THE NATIONAL BANK HAD TO INTERVENE HEAVILY ON EXCHANGE MARKETS ON AUGUST 13, 17 AND 19. IT IS DOING SO IN DM, PRIMARILY IN BRUSSELS, FINANCED BY FECOM (EUROPEAN MONETARY COOPERATION FUND) DRAWINGS WHICH HAVE REACHED AN ESTIMATED BF 25 BILLION SINCE THE CURRENT CRISIS BEGAN LAST MONTH. MORE HEAVY INTERVENTION MAY BE NECESSARY  
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PAGE 03 BRUSSE 08159 201705Z

TODAY (FRIDAY) TO FEND OFF NEW SPECULATION ON A DM REVALUATION OVER THE WEEKEND.

4. IN A PRESS INTERVIEW ON AUGUST 19, NATIONAL BANK GOVERNOR CECIL DE STRYCKER EXPRESSED CONFIDENCE THAT BELGIUM WILL ONCE AGAIN RIDE OUT EXCHANGE MARKET INSTABILITY. DE STRYCKER POINTED TO BELGIUM'S CONTINUING STRONG FOREIGN EXCHANGE RESERVES (BF 217 BILLION) PLUS AVAILABILITY OF FECOM AND IMF

FACILITIES IF NEEDED. HE SAID THAT THE CURRENT SITUATION IS ESSENTIALLY DUE TO GENERAL BELIEF THAT THE DM WILL CONTINUE TO FLOAT UP VIS-A-VIS THE DOLLAR AND OTHER NON-SNAKE CURRENCIES, RATHER THAN TO LACK OF CONFIDENCE IN THE BF ITSELF (AS WAS THE CASE LAST MARCH). DE STRYCKER IS FURTHER QUOTED AS SAYING "PERSONALLY, I DON'T SEE WHAT THE (GERMAN) ELECTIONS CAN CHANGE. GERMANY IS MEETING ITS NORMAL SNAKE OLBIGATIONS, AND HAS NO REASON TO CHANGE ITS POLICY." DE STRYCKER ASCRIBED CURRENT PRESSURES TO PSYCHOLOGICAL RATHER THAN STRICTLY ECONOMIC FACTORS, AND SAID THAT THIS IS ONE OF THE REASONS WHY THE NATIONAL BANK CONTINUES TO BE OPPOSED TO FLOATING EXCHANGE RATES. HE VOWED TO TAKE STRONGER MEASURES IF NECESSARY TO ASSURE THAT BELGIUM REMAINS IN THE SNAKE.

5. PRIVATELY, MIDDLE-LEVEL OFFICIALS AT THE NATIONAL BANK APPEAR SOMWWHAT LESS OPTIMISTIC. THE BELGINA BLANCE OF PAYMENTS AND TRADE INDEED REMAIN AROUND EQUILIBRIUM. MOREOVER, EXPORTS SHOULD INCREASE FASTER IN THE SECOND HALF OF THIS YEAR DUE TO NORMAL CYCLICAL FACTORS. WE HAVE BEEN TOLD IN CONFIDENCE THAT THE BANK IS CURRENTLY ESTIMATING TOTAL LOSS IN FOREIGN EXCHANGE RESEVES FOR THIS CALANDAR YEAR AT BF 40 BILLION; I.E., ABOUL 15 BILLION FROM NOW TO YEAR'S END. WITH SOME SPACING BETWEEN PERIODS OF MARKET UNREST, THESE OFFICIALS BELIEVE THAT BELGIUM COULD CONTINUE TO RIDE THEM OUT INDEFINITELY (FOR EXAMPLE, THE BANK'S BF 34 BILLION IN FECOM BORROWINGS THROUGH LAST MARCH WAS COMPLETELY PAID BACK BY JUNE).

6. THE PROBLEM IS LARGELY ON THE INTERNAL SIDE. THERE IS GENERAL RECOGNITION THAT INTEREST RATES CANNOT LONG REMAIN AT THEIR CURRENT LEVEL WITHOUT DAMAGE TO BELGIUM'S UNCERTAIN ECONOMIC REVIVAL. IF UNCHANGED, THE BANK'S EXTERNALLY ORIENTED MONETARY POLICIES ARE LIKELY TO BECOME A POLITICAL CONFIDENTIAL

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PAGE 04 BRUSSE 08159 201705Z

AND SOCIAL ISSUE HERE, POSSIBLY EVEN BY THE COMMUNAL ELECTIONS IN OCTOBER. NEITHER PUBLIC WEST GERMAN STATEMENTS NOR PRIVATE CONTACTS WITH THE BUNDESBANK GIVE THESE OFFICIALS MUCH HOPE THAT THE GERMANS WILL REVALUE ANY TIME SOON, TAKING BELGIAN AUTHORITIES OFF THIS UNCOMFORTABLE HOOK. NOT SURPRISINGLY, THEREFORE, THERE ARE INDICATIONS OF SERIOUS CONTINGENCY PLANNING GOING ON INTERNALLY WITHIN THE NATIONAL BANK (AND PROBABLY ELSEWHERE IN THE GOVERNMENT) ONE WELL-PLACED AND RESPONSIBLE BANK OFFICIAL HAS TOLD US THAT THE DANISH KRONE IS NOW THE KEY. IF THE DANES LEAVE THE SNAKE IN THE DAYS OR WEEKS AHEAD, HE SAID BLEGIUM AND ITS BENELUX NEIGHBORS WILL BE THE ONLY EC MEMBERS LEFT BESIDES WEST GERMANY. AS SUCH THE VENELUX COUNTRIES WILL HAVE TO RECONSIDER THEIR POSITIONS AS WELL, AT LEAST AS MEMBERS OF THE EXISTING SNAKE.RENNER

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